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IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1972

No. 72-222

LOUISVILLE AND NASHVILLE RAILROAD COMPANY - - - - - - - - - Petitioner

versus

COMMONWEALTH OF KENTUCKY, Ex. Rel. J. E. LUCKETT, Commissioner of Revenue - - - - - - - - - Respondent

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PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF APPEALS OF THE COMMONWEALTH OF KENTUCKY

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August 4, 1972

WESTERN PRINTING CO., INC., 630 W. KENTUCKY, LOUISVILLE, KY.

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IN THE

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LOUISVILLE AND NASHVILLE RAILROAD COMPANY - - - - - - - - - *Petitioner*

v.

COMMONWEALTH OF KENTUCKY, EX. REL. J. E. LUCKETT, Commissioner of Revenue - - - - - - - - - *Respondent*

PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF APPEALS OF THE COMMONWEALTH OF KENTUCKY

Petitioner prays that a Writ of Certiorari issue to review the judgment of the Court of Appeals of the Commonwealth of Kentucky entered in the above entitled case on May 12, 1972.

CITATIONS TO OPINIONS BELOW

The Opinion and Order of the Kentucky Board of Tax Appeals (hereinafter "the Board"), unreported, are printed in Appendix B hereto, *infra,* pp. 17-27. The Franklin Circuit Court, to which appeal was taken from the Board, filed no opinion. The Opinion of the Court of Appeals, printed in Appendix B hereto, *infra,* pp. 28-36), is reported in 479 S. W. 2d 15.

JURISDICTION

The judgment of the Court of Appeals was entered on February 18, 1972. Rehearing was denied on May 12, 1972. The jurisdiction of this Court is invoked under 28 U.S.C., Section 1257(3).

QUESTIONS PRESENTED

1. Did the Court of Appeals of Kentucky, in reversing the judgment of the lower court and the ruling of the administrative agency having jurisdiction, misconstrue the decisions of this Court applying the doctrine of "business situs" and decide this case not in accord with the applicable decisions of this Court?

2. On the facts presented, is it violative of the due process clause of the Fourteenth Amendment of the Constitution of the United States for Kentucky to levy an ad valorem tax on intangible property, the evidences of which are physically and continuously located in the State of New York and subject to the management and control of a company officer having his office only in that state and in the State of Georgia?

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

The constitutional provisions involved are U. S. CONST., amend. XIV, and Ky. CONST., § 192 and § 210. The statutes involved are Kentucky Revised Statutes § 132.190(1)(b) and § 271.145(b). They are printed in Appendix A, *infra,* pp. 15-16.

STATEMENT OF THE CASE

Petitioner is a Kentucky corporation, having its principal office and place of business in Louisville, Kentucky, and engaged in the business of operating a railroad. Petitioner's lines of railroad extend into 12 states. Petitioner has no line of railroad in New York State. Petitioner maintains in New York City an office for the solicitation of traffic and an office from which a substantial part of its financial activities are conducted and supervised.

The Kentucky Department of Revenue (hereinafter "the Department"), having the responsibility of assessing property, both tangible and intangible, of railroad companies owning and operating railroads in Kentucky, assessed Petitioner's property in 1963 for ad valorem tax purposes in Kentucky. Included in the assessment were securities owned by Petitioner but being permanently and continuously located, throughout Petitioner's ownership thereof, in New York City. The securities included notes, certificates of deposit, and state and municipal bonds. Petitioner duly protested the assessment, which, however, was made final by the Department in the amount of $19,698,151. Petitioner appealed to the Board, which reversed the final action of the Department, and found the securities to have a business situs in New York City and thus not to be taxable in Kentucky. The Department appealed to the Franklin Circuit Court, which affirmed the action of the Board. The Department then appealed to the Kentucky Court of Appeals, which reversed.

Petitioner's New York financial office is in charge of Petitioner's Vice President-Finance, who resides in Atlanta, maintains an office in Atlanta, and has no office in Kentucky. He is the custodian of Petitioner's funds and securities in the City of New York and is responsible for all financial requirements of Petitioner, including the buying, selling and management of securities. The New York financial office has existed since at least 1879, and the business of that office has been carried on since that time.

Funds generated from the securities invested in by Petitioner and not needed in the day-to-day operation of the railroad are retained in New York and reinvested; funds generated in the operations of Petitioner and not needed in the day-to-day operation of the railroad are sent to New York and are there employed in the purchasing of securities. Separate books and accounts are maintained and kept in New York. At the close of 1962 (the time of assessment involved in this case), the value of securities owned by Petitioner and held under the management of the Vice President-Finance in New York aggregated $43 million. The year-end totals for the ten-year period preceding 1962 showed little variation from that amount.

During the year 1963, there were 185 separate purchase transactions of securities aggregating $67,055,000; 109 sales, aggregating $55,734,000; and 37 redemptions, aggregating $14,748,000. Transactions concerning such securities occur almost daily. The types of securities which are traded include repurchase agreements, commercial paper, certificates

of deposit, United States Government securities, and municipal bonds. The current obligations of Petitioner and the need of funds to meet them are one of the factors considered by the Vice President-Finance in making investments.

In 1963, Petitioner's securities transactions produced a gross income of $1,678,214, of which $474,978 represented capital gains profits. The profit from the securities transactions are used to pay the expenses of the New York office, for reinvestment in securities and for other uses which Petitioner might decide upon. The New York office maintains a number of bank accounts on which only certain officers of Petitioner in New York may draw, no other officer of Petitioner than those designated ones in New York being allowed to draw on the New York accounts, except the one in which are deposited funds for dividends to stockholders. The securities in question were physically located in New York during the period of Petitioner's ownership thereof and were never in Kentucky.

The financial office of Petitioner is located in New York for the reason that the financial business of Petitioner can be most expeditiously and beneficially handled from there. Decisions governing transactions concerning the securities in issue are independently arrived at by the Vice President-Finance, and are not dependent upon decisions made at Petitioner's headquarters in Kentucky. The day-to-day management of the securities is the responsibility of the Vice President-Finance, although the Executive Committee of

Petitioner's Board of Directors has general supervision of them. The Executive Committee holds its meetings in New York—with the exception of the month of April, when it meets in Kentucky—and only one of the five members of that Committee is domiciled in Kentucky. During 1963, as was its traditional and annual custom, Petitioner's Board of Directors met in New York with the exception of April, in which month it met in Kentucky, and August, in which month it did not meet.

While certain securities owned by Petitioner are held in Kentucky, they are of a different character from those held in New York and Kentucky ad valorem tax was paid upon them. The day-to-day operating expenses of Petitioner are paid from bank accounts under the control of Petitioner's Treasurer, whose office is in Kentucky, and who has no authority over bank accounts under the control of the New York office.

In disposing of the case, the Court of Appeals said, *infra*, pp. 33-34:

> "In our opinion the evidence required the conclusion that while the buying and selling of securities by the L&N in New York constitute business transactions, they do not amount to a separate and independent securities business in New York. This is not to say that in order for a business to come within the integration doctrine or to have a business situs it must have no connections at all with the individual or corporation that happens to be its owner. We are saying that each case must be examined to determine if the elements

present are such as to establish that the nondomiciliary business activities are a separate entity and independent from the business of the domiciled corporation.

"The L&N's contention that its securities business in New York is a separate and independent business enterprise is not compatible with the position it must maintain to stay in conformity with the Constitution of the Commonwealth of Kentucky. Section 210 of our Constitution states:

> 'No corporation engaged in the business of common carrier shall, directly or indirectly, own, manage, operate or engage in any other business than that of a common carrier, or hold, own, lease or acquire, directly or indirectly, mines, factories or timber, except such as shall be necessary to carry on its business; and the general assembly shall enact laws to give effect to the provisions of this section.'

"Section 192 of our Constitution prohibits a corporation from engaging in any business other than that expressly authorized by its charter, and KRS 271.145(1) prohibits any corporation from engaging in any business other than that expressly authorized by its articles of incorporation.

"In our opinion the L&N does have the power to buy and sell securities to facilitate its corporation purposes as a common carrier. However, consistently with the above constitutional and statutory prohibitions, the L&N cannot maintain that it is operating an independent and separate securities business having a business situs, under all this term implies, in New York or anywhere else."

The federal question in this case, i.e., whether the action of the Department in assessing intangibles for the purposes of property taxation deprived Petitioner of due process of law, as guaranteed by the Fourteenth Amendment to the Constitution of the United States, was first raised before the Board, the body possessing initial jurisdiction to review the action of the Department. The question was raised by Petitioner's explicit reliance in its Petition for Review to the Board upon the doctrine of "business situs". The Board took this argument under consideration and dealt with it in its opinion, saying "The location of property is generally known in law as its 'situs'. For purposes of due process within the meaning of the Fourteenth Amendment to the United States Constitution, it is necessary for a state to have jurisdiction over the 'situs' of property to subject it to taxation." *Infra*, p. 20. Inasmuch as petitioner prevailed before the Board, the Department appealed to the Franklin Circuit Court and Petitioner, in its answer to the appeal, simply denied the allegations that the order of the Board was erroneous. In the Franklin Circuit Court, Petitioner continued to rely upon the doctrine of "business situs" and was sustained. In its notice of appeal to the Court of Appeals, the Department appealed from that part of the order and judgment of the Franklin Circuit Court which dismissed the Department's appeal from so much of the order of the Board holding the intangible personal property of Petitioner to have "acquired a business situs in the State of New York". In the Court of Appeals, Pe-

titioner continued to rely upon the doctrine of "business situs" and upon the contention that its intangible personal property at issue in this proceeding had acquired a business situs in the State of New York. The Court of Appeals ruled that such a business situs had not been acquired.

Thus, the federal question was raised in the initial forum having jurisdiction to review the Department's actions complained of by Petitioner, *Braniff Airways, Inc.* v. *Nebraska State Board of Equalization and Assessment, et al.*, 347 U. S. 590 (1954), and the case was practiced on that issue from the outset to the present time.

REASONS FOR GRANTING THE WRIT

This Court's decisions and opinions in *New Orleans* v. *Stempel*, 175 U. S. 309 (1899); *Bristol* v. *Washington County*, 177 U. S. 133 (1900); *State Board of Assessors* v. *Comptoir National d'Escompte*, 191 U. S. 388 (1903); *Metropolitan Life Insurance Company of New York* v. *City of New Orleans*, 205 U. S. 395 (1907); and *New York ex rel. Whitney* v. *Graves, et al.*, 299 U. S. 366 (1937), show that one's affairs may be so conducted as to result in a localization of property in a state other than that of the residence of the owner and that this will preclude ad valorem taxation of that property other than at the state of its location and permit taxation by the state in which the property has become localized. The Kentucky Court of Appeals, on facts sufficient to have persuaded the Board and the initial reviewing court to find the situs

of the intangible personal property to be in New York, reversed the earlier holdings and found the situs to be in Kentucky. It held that Petitioner, because of constitutional and statutory limitations on its power to do business, could not conduct a "securities business" in New York or anywhere else, and thus that the situs could not be in New York. In reaching that conclusion, the Court wholly misconstrued the holdings of this Court in the cases cited above. The Court of Appeals interpreted those cases to mean that business situs can only be acquired if the activities under scrutiny constitute a "business" in the corporate charter sense. In fact, the opinions of this Court show that a series of transactions long-conducted on a localized basis is sufficient to preclude or permit ad valorem taxation, as the case may be, bringing into play the doctrine of "business situs".

The maxim *mobilia sequuntur personam*—it being a fiction—has not been allowed to prevail over facts and circumstances in a particular case which dictate a result different from that to which the fiction points. Referring to its frequent declarations to that effect, the Court said in *DeGanay* v. *Lederer, Collector of Internal Revenue,* 250 U. S. 376, 382 (1919): ". . . notes, bonds and mortgages may acquire a situs at a place other than the domicile of the owner, and be there reached by the taxing authority". Commenting that the securities before it in that case—the owner being a citizen of France—were in the United States, that they were held by an agent having authority to sell, assign, or transfer and to invest and reinvest the pro-

ceeds of sale as it might deem best in the interest of the principal, the Court went on to say that it was difficult to conceive how property could be more completely localized in the United States. So, in the instant case, the bonds, certificates of deposit and notes are held in New York City, and are managed by an officer of the Company having authority to sell, assign or transfer any of them and to invest and reinvest the proceeds of the sale as he might deem best in the management of the affairs of Petitioner.

In *Bristol* v. *Washington County, supra,* the Court was influenced, in holding that Minnesota could tax notes and mortgages in which the owner's agent had invested in Minnesota, the owner being a resident of New York, by the holding of the Minnesota Supreme Court that the property was in Minnesota not for a temporary purpose but "as permanently as though the owner resided here", 177 U. S. at 142; that the investments were employed in Minnesota as a business, that they were exclusively under the protection of Minnesota's laws and that the laws of New York had never operated upon them. The fact that in the latter days of her activity, the owner had directed that the notes be sent to her in New York did not dictate a different result. In the instant case, the securities owned by Petitioner are permanently in the City of New York and have been employed in that City as a business, using that word in the sense of a long continued series of transactions devoted toward producing a profit; they have been exclusively under the protection of the laws of New York and the laws of the State of Kentucky have never operated upon them.

A comment apropos to the meaning of the term "business situs" appears in *New York ex rel. Whitney* v. *Graves, supra,* at p. 372: "When we speak of a 'business situs' of intangible property in the taxing State we are indulging in a metaphor. We express the idea of localization by virtue of the attributes of the intangible right in relation to the conduct of affairs at a particular place. The right may grow out of the actual transactions of a localized business or the right may be identified with a particular place because the exercise of the right is fixed exclusively or dominantly at that place. In the latter case the localization for the purpose of transacting business may constitute a business situs quite as clearly as the conduct of the business itself".

It is difficult to see how the facts of this case might have persuaded the Kentucky Court of Appeals—had it actually decided the question of business situs on the facts relative to the securities rather than having decided it on the question of the power of Petitioner—to have reached a conclusion other than that the securities at issue are localized in New York City and do have a business situs there, thus taking them beyond the taxing power of Kentucky in accordance with the provisions of KRS § 132.190(1)(b). Kentucky affords no protection to the securities or to the activities of Petitioner's officers in New York City in their execution of securities transactions; the benefits of the investment and the opportunities to make the investments come from compliance with the laws of the State of New York. The transactions in which the invest-

ments were used were identified with New York; the securities were held there not just for safekeeping but as well for collection of income and principal and for reinvestment. Surely they could not have been more completely localized anywhere.

If the interpretation of the Court of Appeals of Kentucky were to gain adherents the protection of the Fourteenth Amendment would be greatly diluted, the mis-construction of the rulings of this Court in the field would spread and the reach of the state tax gatherer would extend beyond the scope allowed by the Fourteenth Amendment. Great numbers of multi-state corporations engage in investment activity such as that described in this proceeding. It is important to them—and to the several states in the administration of their tax laws—that the Supreme Court make explicit the teaching of its opinions on the point upon which the Court of Appeals ruled below. Without that explicitness, a corporation investing its funds on a continuous and permanent basis in a state other than those of its incorporation and domicile would find at least the domiciliary state seeking to reach the securities representing the investment on the grounds that only the clear inclusion in the corporate charter of a power to engage in the business of buying and selling securities would be sufficient to preclude its own taxing power. This, it is submitted, would be a delimitation upon the doctrine of "business situs" as explicated by decisions of this Court which can find no sanction in those decisions.

CONCLUSION

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

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August 4, 1972

APPENDIX

APPENDIX

APPENDIX A

CONSTITUTION OF THE UNITED STATES

AMENDMENT XIV

Section 1

All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State wherein they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

CONSTITUTION OF KENTUCKY

Section 192

Business unauthorized by charter prohibited; real estate.—No corporation shall engage in business other than that expressly authorized by its charter, or the law under which it may have been or hereafter may be organized, nor shall it hold any real estate, except such as may be proper and necessary for carrying on its legitimate business, for a longer period than five years, under penalty of escheat.

Section 210

Common carrier not to engage in any other business.—No corporation engaged in the business of common carrier shall, directly or indirectly, own, manage, operate or engage in any other business than that of a common carrier, or hold, own, lease or acquire, directly or indirectly, mines,

factories or timber, except such as shall be necessary to carry on its business; and the general assembly shall enact laws to give effect to the provisions of this section.

KENTUCKY REVISED STATUTES

Section 132.190(1)(b)

Property subject to taxation; situs.

(1) The property subject to taxation, unless exempted by the Constitution, shall be as follows:

* * * * * * *

(b) All intangible personal property of individuals residing in this state and of corporations organized under the laws of this state unless it has acquired a business situs without this state.

Section 271.145(1)

Limitations on business and holding of real estate; escheat procedure.

(1) No corporation shall engage in business other than that expressly authorized by its articles of incorporation, or the law under which it was organized, nor shall it hold any real estate, except such as may be proper and necessary for carrying on its legitimate business, for a longer period than five years, under penalty of escheat.

APPENDIX B

KENTUCKY BOARD OF TAX APPEALS

No. 64-R-6

LOUISVILLE AND NASHVILLE RAILROAD COMPANY - *Appellant*

v.

DEPARTMENT OF REVENUE, COMMONWEALTH OF KENTUCKY - - - - - - - *Appellee*

ORDER No. K-776—Entered March 16, 1967

This is an appeal from a final ruling dated March 2, 1964, of the Department of Revenue confirming an assessment in the sum of $66,808.66 for ad valorem taxes for the year 1963 against appellant, L & N Railroad Company.

Appellant, L & N Railroad Company, filed its schedule of property subject to Kentucky ad valorem taxation for the year 1963. It listed thereon certain intangible property as not being subject to Kentucky ad valorem taxation. Appellee, Department of Revenue, reviewed the schedule, determined that excluded intangible property of the value of $26,723,464.00 was subject to Kentucky ad valorem taxation and issued an additional assessment in the amount of $66,808.66. This assessment was protested and the Department of Revenue confirmed its assessment by final ruling dated March 2, 1964. This appeal timely followed.

The issues presented on this appeal are:

I. Whether certain intangible property owned by appellant has acquired a "business situs" in New York

and is thus not subject to Kentucky ad valorem taxation under KRS 132.190 (1) (b)? This issue involves intangible property of the value of $19,698,151.00.

II. Whether appellant which has transferred or pledged securities or other intangible property to a non-resident trustee under a deed of trust or other trust agreement retains sufficient indicia of ownership to subject said securities or other intangible property to Kentucky ad valorem taxation against appellant? This issue relates to intangible property in the amount of $6,745,888.00, including $2,390,676.00 in stock owned by appellant in the Nashville and Decatur Railroad Company.

III. Whether appellant, as a shareholder of stock in another railroad is liable for ad valorem taxes on the shares held by it? This issue relates to stock in the Nashville and Decatur Railroad Company owned by appellant in the amount of $2,670,101.00, of which amount $2,390,676.00 is also involved in the second issue presented in this case. Appellant contends that the Nashville and Decatur Railroad Company properties were included in its return for 1963 as a part of its properties under the "unit" requirement of KRS 136.160 and the stock is thus exempt under KRS 136.030(1).

The pertinent facts and our conclusions on those issues are as follows:

I

Appellant, Louisville and Nashville Railroad Company, is a Kentucky corporation with its main office at Louisville, Kentucky. It has no railroad lines in New York but it has maintained for many years an office in New York, New

York. C. R. Yates, Vice President-Finance, is in charge of the New York Office. He also maintains an office in Atlanta, Georgia, but has no office in Kentucky. He has responsibility for all financial requirements of appellant, including the buying, selling and management of securities, subject to the ultimate authority of appellant's Board of Directors and Executive Committee.

Funds not used in the day-to-day operation of the railroad are sent to the New York Office. As a recognized business practice, appellant must maintain surplus funds to meet financial obligations and contingencies. To derive maximum benefit from these surplus funds, when not otherwise needed, they are used in the buying and selling of securities by the New York office. While day-to-day operating expenses are paid by the Treasurer at Louisville, liabilities of appellant such as trust obligations are paid by the New York Office as they accrue.

The value of cash and securities held under the management of the Vice President-Finance in New York at the close of 1962 totaled approximately $43,000,000.00, including tax exempt government obligations. Year end values of cash and securities had been relatively constant for a number of years. This sum also represented the approximate value of cash and securities at the end of 1963. During the year 1963, the sum of approximately $33,000,000.00 was forwarded by the Treasurer in Louisville to the New York office. In the year 1963, a typical year, there were 185 separate purchase of securities transactions totaling $67,055,000.00, 109 sales aggregating $55,734,000.00 and 37 redemptions totaling $14,748,000.00. The securities business of appellant had a gross income of $1,678,214.00 for the year 1963.

Funds controlled by the New York office, as well as income from the investment business, were used to pay the expenses of the New York office, for reinvestment in the

securities business and to pay obligations of the appellant. Since the value of cash and securities held under the management of the New York office at the end of 1962 was approximately the same as that at the end of 1963, we concluded that the $33,000,000.00 forwarded by the Treasurer during the year 1963 to the New York office and the gross income of $1,678,214.00 from the securities business for the year 1963 were used for two purposes, namely, payment of expenses of the New York office and payment of liabilities such as trust obligations and dividends of appellant.

The location of property is generally known in law as its "situs." For purposes of due process within the meaning of the Fourteenth Amendment to the U. S. Constitution, it is necessary for a state to have jurisdiction over the "situs" of property to subject it to taxation.

Normally, intangibles are taxable at the legal domicile of the owner on the basis of the Roman maxim "mobilia sequuntur personam" (movable things, or movables follow the person) which, in the case of a corporation, is the state of incorporation. A recognized exception to this rule is that if the intangibles are used in a non-domiciliary state, that state may tax such intangibles on the basis of a "business situs" acquired there. Guaranty Trust Co., of N. Y. v. Virginia, 305 U. S. 19, 59 S. Ct. 1. A further exception is that where the business of a corporation is so localized as to its commercial practices as to be actually managed and functioning in a state other than the state of incorporation, though its activities reach into two or more states, there may be for tax purposes a "commercial domicile" sufficient to permit the state where the corporation has its chief place of business, and where the management functions are exercised, to tax all of the intangibles of the corporation. Wheeling Steel Corporation v. Fox, 298 U. S. 193, 80 L. ed. 1143, 56 S. Ct. 733.

The general rule for taxation of intangibles and "business situs" exception are embodied in KRS 132.190(1) (b), which provides:

> "(1) The property subject to taxation, unless exempted by the Constitution, shall be as follows: . . . (b) All intangible personal property of individuals residing in this state unless it has acquired a business situs without this state."

In Commonwealth v. Madden, 265 Ky. 634, 97 S. W. 2d 561, it was held that the Commonwealth of Kentucky had no power to subject to ad valorem taxation the interest of a resident in the assets of a partnership (the other members being non residents of Kentucky) engaged in buying and selling securities on the New York Stock Exchange. All of the partnerships accounts were carried with brokers in New York, the securities purchased and sold were carried in the names of New York brokers and trading was almost universally carried on in person at the brokerage offices. The court declared that there was such a localization of the assets in New York as to give them an exclusive situs for property taxation in New York.

The term "business situs" according to numerous decisions, is not the subject of precise definition. It appears to apply generally to a situs at a place other than the domicile of the owner, where an agent, manager or the like, is conducting a separate business where intangibles are used as a part of the local business. The trend of modern decisions is to rely upon the "integration doctrine" to identify the existence of a business situs. Under the doctrine, it is necessary that the intangibles become an integral part of some business activity and that their control be localized in some independent business.

We think the intangibles in question had acquired a business situs in New York and were not subject to ad valorem

taxation here. The assessment made by the appellee related to a part of the average amount or value of intangibles habitually and continuously located and used in New York for a number of years in the investment business.

Our answer to the first issue is thus in the affirmative.

II

"(1) The property subject to taxation, unless exempted by the Constitution, shall be as follows:

(a) All real and personal property within this state, including intangible personal property of nonresidents and corporations not organized under the laws of this state that has acquired a business situs within this state, except that twenty five domestic fowls to each family shall be exempt from taxation for any purpose.

(b) All intangible personal property of individuals residing in this state and of corporations organized under the laws of this state unless it has acquired a business situs without this state.

(2) The property enumerated in paragraph (b) of subsection (1) of this section shall be considered and estimated in fixing the valuation of corporate franchises.

(3) Property shall be assessed for taxation at its fair cash value, estimated at the price it would bring at a fair voluntary sale.

(4) The situs of intangible personal property for purposes of taxation shall be at the residence of the real or beneficial owner, and not at the residence of the fiduciary or agent having custody or possession."

In City of Henderson v. Barrett's Ex'r, 152 Ky. 648, 153 S. W. 992, it was said:

"That ordinary intangible personal property follows the person of the owner, but that its situs may be fixed

by the Legislature of the state. If the Legislature sees fit to fix the situs of such property at the residence of the trustee, it may do so; on the other hand, if it sees fit to fix the situs at the residence of the beneficial owner, that power cannot be denied."

Under the present statute, intangible property is taxable at the domicile of its real or beneficial owner unless it has acquired a business situs elsewhere. This is true of either a resident or non resident. Commonwealth v. Sun Life Assurance Co., 170 S. W. 2d 895; Standard Oil Company v. Commonwealth, 311 S. W. 2d 372. The real or beneficial owner of the intangibles in question here is the appellant.

Appellant relies principally upon two cases as decisive on this issue. We do not agree.

One case is Safe Deposit & Trust Co. of Baltimore v. Commonwealth of Virginia, 280 U. S. 83, 74 L. ed. 180, 50 S. Ct. 59. In that case a resident of Virginia transferred intangibles to a bank in Baltimore in trust for his two minor children. Upon attaining 25 years of age, each was to receive one-half of the trust estate with accumulations. After the death of the trustor or settlor, the Commonwealth of Virginia sought to impose an ad valorem tax on the corpus of the trust. The entity sought to be taxed was the non-resident trustee. The right to tax was denied. In the opinion it was said:

"The power of Virginia to lay a tax upon the fair value of the interest in the securities actually owned by one of her resident citizens is not now presented for consideration."

The other case is Commonwealth v. Appalachian Electric Power Co., 159 Va. 462, 166 S. E. 461, cert. den. 288 U. S. 613. In that case a power company domiciled in Virginia transferred certain bonds to a New York bank as

trustee to secure a loan. Virginia attempted to levy a tax on the bonds. Its right to do so was denied. The court therein stated:

> "The fact that the State of New York imposes no such tax on this class of property is immaterial. The controlling question is; Has that state the right to tax the property? We think it has. If so, Virginia, under the decisions, has no such right."

Shortly after this decision the U. S. Supreme Court decided Curry v. McCanless, 307 U. S. 357, 83 L. ed. 1339, 59 S. Ct. 900. It appears that this case is contrary to the Appalachian Electric Power Co., case insofar as the latter stands for the proposition that taxation in one state excludes the right of any other state to tax. It was therein said:

> "In cases where the owner of intangibles confines his activity to the place of his domicile it has been found convenient to substitute a rule for a reason, cf. New York ex rel. Cohn v. Graves, 300 U. S. 308, 313, 81 L. ed. 666, 670, 57 S. Ct. 466, 108 A. L. R. 721; First Bank Stock Corp. v. Minnesota, 301 U. S. 234, 241, 81 L. ed. 1061, 1065, 57 S. Ct. 677, 113, A. L. R. 228, by saying that his intangibles are taxed at their situs and not elsewhere, or, perhaps less artificially, by invoking the maxim mobilia sequuntur personam, Blodgett v. Silberman, 277 U. S. 1, 72 L. ed. 749, 48 S. Ct. 410, supra; 1056, 50 S. Ct. 436, 72 A. L. R. 1303, supra, which means only that it is the identity or association of intangibles with the person of their owner at his domicile which gives jurisdiction to tax. But when the taxpayer extends his activities with respect to his intangibles, so as to avail himself of the protection and benefit of the laws of another state, in such a way as to bring his

person or property within the reach of the tax gatherer there, the reason for a single place of taxation no longer obtains, and the rule is not even a workable substitute for the reasons which may exist in any particular case to support the constitutional power of each state concerned to tax. Whether we regard the right of a state to tax as founded on power over the object taxed, as declared by Chief Justice Marshall in McCulloch v. Maryland, 4 Wheat. 316, 4 L. ed. 579, supra, through dominion over tangibles or over persons whose relationships are the source of intangible rights, or on the benefit and protection conferred by the taxing sovereignty, or both, it is undeniable that the state of domicile is not deprived, by the taxpayer's activities elsewhere, of its constitutional jurisdiction to tax, and consequently that there are many circumstances in which more than one state may have jurisdiction to impose a tax and measure it by some or all of the taxpayer's intangibles. Shares of corporate stock may be taxed at the domicile of the shareholder and also at that of the corporation which the taxing state has created and controls; and income may be taxed both by the state where it is earned and by the state of the recipient's domicile. Protection, benefit, and power over the subject matter are not confined to either state. The taxpayer who is domiciled in one state but carries on business in another is subject to a tax there measured by the value of the intangibles used in his business. New Orleans v. Stempel, 175 U. S. 309, 44 L. ed. 174, 20 S. Ct. 110; Bristol v. Washington County, 177 U. S. 133, 44 L. ed. 701, 20 S. Ct. 585; State Assessors v. Comptoir Nat. D'Escompte, 191 U. S. 388, 48 L. ed. 232, 24 S. Ct. 109; Metropolitan L. Ins. Co. v. New Orleans, 205 U. S. 395, 51 L. ed. 853, 27 S. Ct. 499; Liverpool & L. & G. Ins. Co. v. Board of Assessors, 221 U. S. 346, 55 L. ed. 762, 31 S. Ct. 550, L. R. A. 1915 C. 903; Wheel-

ing Steel Corp. v. Fox, 298 U. S. 193, 80 L. ed. 1143, 56 S. Ct. 773; cf. Blodgett v. Silberman, 277 U. S. 1, 72 L. ed. 749, 48 S. Ct. 410, supra; Baldwin v. Missouri, 281 U. S. 586, 74 L. ed. 1056, 50 S. Ct. 436, 72 A. L. R. 1303, supra. But taxation of a corporation by a state where it does business, measured by the value of the intangibles used in its business there, does not preclude the state of incorporation from imposing a tax measured by all its intangibles. Cream of Wheat Co. v. Grand Forks County, supra (253 U. S. 329, 64 L. ed. 934, 40 S. Ct. 558); see Fidelity & C. Trust Co. v. Louisville, 245 U. S. 54, 62 L. ed. 145, 38 S. Ct. 40, L. R. A. 1918C, 124.

The intangibles, being temporarily in another state for the purpose of securing loans, did not fall within the classification of property with a business situs outside this state.

The intangibles in question were properly taxable here and the second issue is answered in the affirmative.

III

In our opinion, the stock of the Nashville and Decatur Railroad Company owned by appellant is not exempted from ad valorem taxation under KRS 136.030. Although the property of the Nashville and Decatur Railroad Company was taken into consideration as a part of the properties of the L & N R. Co., under the unit requirement of KRS 136.360, it does not follow that the Nashville and Decatur Railroad Company or anyone else, including appellant, has paid ad valorem taxes to the Commonwealth of Kentucky on at least seventy five (75%) percent of its total property, wherever located.

We therefore answer the third question in the affirmative.

IT IS THEREFORE ORDERED by the Kentucky Board of Tax Appeals that the final action of the Department of Revenue dated March 2, 1964, against appellant, L & N Railroad Company, is reversed as to the first issue presented herein, and is affirmed as to the last two issues presented herein. This cause is remanded to the Department of Revenue for entry of an assessment consistent with this order.

This 16th day of March, 1967.

KENTUCKY BOARD OF TAX APPEALS

(s) Jack T. Page
Chairman

Attest:
Ellis A. Merrifield, Clerk

By:

(s) Margaret Bennett
Acting Clerk

Spragens, Robert M., not sitting.

COURT OF APPEALS OF KENTUCKY

COMMONWEALTH OF KENTUCKY, EX REL. J. E. LUCKETT, Commissioner of Revenue, - - - - - - - - - - *Appellant,*

v.

LOUISVILLE & NASHVILLE RAILROAD COMPANY and KENTUCKY BOARD OF TAX APPEALS, - - *Appellees.*

AND

LOUISVILLE & NASHVILLE RAILROAD COMPANY, - - - - - - - - - *Cross-Appellant,*

v.

COMMONWEALTH OF KENTUCKY, EX REL. J. E. LUCKETT, Commissioner of Revenue, - - - - - - - - - *Cross-Appellee.*

No. S-115-70

February 18, 1972

Rehearing Denied May 12, 1972

NEIKIRK, Judge.

The Louisville & Nashville Railroad Company (hereinafter referred to as L & N), a Kentucky corporation, engaged in the business of a common carrier and having its principal office in Louisville, Kentucky, filed with the Commonwealth of Kentucky, Department of Revenue (here-

inafter referred to as Department of Revenue), its schedule of property subject to ad valorem taxes for the year 1963. The L & N reported certain intangible property located outside of Kentucky in the amount of $26,723,464 as not being subject to Kentucky ad valorem taxes. The Department of Revenue reviewed the return and determined that the listed intangible property was subject to be taxed and requested payment from the L & N of additional taxes due in the sum of $66,888.66.

The L & N appealed the additional assessment to the Kentucky Board of Tax Appeals. The L & N contended that $19,698,151 of the intangible property was not taxable by Kentucky because it was used in a separate and independent business and had acquired a business situs in the city of New York; and that the remaining $7,025,313 in intangibles was not taxable in Kentucky for various other reasons.

The Kentucky Board of Tax Appeals held that the intangibles in the custody of the L & N office in New York in the amount of $19,698,151 had acquired a business situs outside of Kentucky and, therefore, were not subject to taxation by Kentucky. The Department of Revenue perfected an appeal to the Franklin Circuit Court from this portion of the Board's order. The Board held that the remaining $7,025,313 of intangibles was subject to the ad valorem tax under KRS Chapter 132. The L & N attempted to appeal this portion of the Board's order by filing a cross-appeal in the Franklin Circuit Court. The Department of Revenue moved that the cross-appeal be dismissed, pointing out that it had not been timely filed. The Franklin Circuit Court did not pass on this motion, but entered judgment affirming the Board's order in all respects. The Department of Revenue appeals to this court from the portion of the judgment that affirmed the Board's order that the intangibles in the L & N's office in the city of New York had

acquired a business situs and were not taxable in Kentucky. The L & N filed a cross-appeal in this court from the portion of the judgment that affirmed the Board's order that all other intangibles in dispute were taxable. The Department of Revenue moved to dismiss the cross-appeal. By an order we directed that the motion to dismiss the cross-appeal be passed for consideration on the merits, which we now shall proceed to do.

The order of the Kentucky Board of Tax Appeals was entered on March 16, 1967. It was not until April 20, 1967, that the L & N attempted to appeal that portion of the final decision of the Board adverse to L & N. KRS 131.370 requires an adverse decision of the Board of Tax Appeals be appealed to the Franklin Circuit Court within thirty days. Thus, the attempted appeal designated as "cross-appeal" was not timely filed. The L & N contends that a cross-appeal is not essential in order to present an issue that is an element of, or one closely related in substance to, the question properly presented by the other party. In the instant case, the Department of Revenue had convinced the Kentucky Board of Tax Appeals that the L & N's intangibles, other than those held in the New York office, were subject to be taxed. The Department of Revenue did not attempt to fragment appellate review by selectively designating special findings of the Board, but appealed from that portion of the final order of the Board adverse to the Department of Revenue. It was incumbent upon the L & N to appeal to the Franklin Circuit Court that portion of the Board's order adverse to the L & N's contentions in order to vest jurisdiction in the Franklin Circuit Court as to these issues. The L & N evidently considered this to be sound by filing a cross-appeal in the Franklin Circuit Court and a cross-appeal in this court. The L & N could have perfected a direct appeal from that portion of the Board's order adverse to its claims. Had the L & N

chosen this route and no appeal had been taken by the Department of Revenue, the Franklin Circuit Court would have had jurisdiction to dispose of the cause without reference to other issues not properly reserved and presented. The Franklin Circuit Court was without jurisdiction to hear and determine any issues other than those perfected by appeal of the Department of Revenue. Commonwealth, Dept. of Highways v. Berryman, Ky., 363 S. W. 2d 525 (1962); Kentucky Department of Revenue v. Summers-Herrmann, Inc., Ky., 453 S. W. 2d 543 (1970).

The Franklin Circuit Court erred in failing to dismiss the L & N's cross-appeal to that court. However, the net effect of the circuit court's judgment was the same as if the cross-appeal had been dismissed, so we are affirming that judgment on the L & N's cross-appeal to this court.

The issue squarely presented to the Franklin Circuit Court and now to this court is whether or not the intangibles owned by the L & N and physically located in an office in New York City are subject to the ad valorem tax imposed by the Commonwealth of Kentucky.

KRS 132.190(1) (b) provides:

> "(1) The property subject to taxation, unless exempted by the Constitution, shall be as follows:"
>
> * * * * * * *
>
> "(b) All intangible personal property of individuals residing in this state and of corporations organized under the laws of this state unless it has acquired a business situs without this state."

The L & N contends that the activities of the New York office are such as to bring the intangibles there held under the above-quoted statutory exception.

The question of "business situs" presents a problem. It is difficult to formulate a consistent workable rule for determining if intangibles physically located outside the

state of a domiciled owner corporation are subject to be taxed by the domiciliary state. As a general rule, intangibles are taxable at the legal domicile of the owner on the theory of the Roman maxim "mobilia sequuntur personam": movables follow the owner. A recognized exception to this rule is that if the intangibles have become an integral part of some local independent and separate business activity and their possession and control are localized in a nondomiciliary state, then the intangibles have acquired a business situs apart from the owner's domicile. This is known as the "integration doctrine." Wheeling Steel Corp. v. Fox, 298 U.S. 193, 56 S.Ct. 773, 80 L.Ed. 1143 (1936).

The reasoning behind the establishment and growth of the integration doctrine is sound, and we do not question its validity; nor do the parties. However, in any determination of the establishment of a business situs, the facts in each case must be examined. Generally speaking, courts have agreed that certain elements must be present in order for the courts to recognize the existence of a business situs of intangible property under the integration doctrine. There must be a general or more or less continuous course of business; a permanency of location of the intangibles; independent control and management as distinguished from mere custody for safekeeping; possession and control by an independent local agent who holds the intangibles for the purpose of transacting a permanent business; and the business or investments in the nondomiciliary state must be so established and used in such a fashion that the substantial use and value of the intangibles become attached to and become an asset of the business outside the domicile of the owner. See 143 A.L.R. 361.

The L & N for many years has maintained surplus funds not needed in its day-to-day railroad obligations. In order to reap the greatest benefit possible out of this surplus, the L & N uses these funds to purchase securities. For many

years there has been approximately $43,000,000 employed as capital in this endeavor. We have no quarrel with the L & N's position that it has a legal right to buy and sell and trade in securities for its own account. KRS 271.125(10). These activities may be properly classified as a business. KRS 139.040. Kales v. Commissioner of Internal Revenue, 6 Cir., 101 F.2d 35 (1939). This does not mean, however, that the L & N's investment activities constitute a business enterprise separate from and independent of the overall railroad business activities of the L & N.

The L & N contends that its securities business in New York meets the requirements that courts have considered essential in determining business situs, by reason of these facts: (1) for the purpose of carrying on the securities business, the L & N maintains an office in New York; (2) the books concerning the activities of the office are kept in New York; (3) the Board of Directors and Executive Committee of the company hold meetings in New York; (4) the day-to-day management of the securities in New York is the responsibility of the Vice President-Finance Agent, a resident of New York; (5) the intangible property is physically located there; (6) the income from the securities business is received in New York; (7) all accounts are kept in New York banks; (8) the authority to draw on these accounts is vested in the New York agent; (9) the expenses in connection with the activities of the office are paid from accounts in New York banks; (10) the agent has independent management of the securities; (11) the securities enterprise is of a permanent and continuous nature; and (12) the intangible personal property sought to be taxed is part of and is connected with a local business in New York.

The L & N cites Commonwealth v. Madden's Ex'r, 265 Ky. 684, 97 S.W.2d 561 (1936), and Standard Oil Company v. Commonwealth ex rel. Allphin, Ky., 311 S.W.2d 372 (1957), as reliable authorities for its position that the intangibles have acquired a business situs in New York.

In Madden, we held that the Commonwealth of Kentucky had no power to subject to ad valorem taxation the interest of a Kentucky resident in the assets of a brokerage partnership owned in part by the Kentucky resident and located in New York. The assets that made up the brokerage firm were located in New York and completely controlled by an office there. Kentucky's only relationship was that Madden, from time to time, lived in Kentucky. The sole business of the partnership was the buying and selling of securities, and all activities were conducted exclusively in New York. These facts supported the finding that the partnership brokerage firm had established a business situs and was domiciled in New York. The instant case is distinguishable on the admitted facts.

In the Standard Oil Company case, supra, this court said:

> "The primary issue on this appeal is whether this State can constitutionally levy an ad valorem tax upon the accounts and notes receivable and bank deposits of the appellant, Standard Oil Company, a Kentucky corporation, which intangibles admittedly have a business situs in other States."

Unlike in the instant case, the business situs of the intangibles belonging to the Standard Oil Company was admitted to be outside the jurisdiction of Kentucky and, therefore, the intangibles were not subject to be taxed by Kentucky. The Standard Oil Company case is not controlling here, as the "business situs" is the battleground of the antagonists.

In our opinion there are elements present in this case that override the factors relied upon by the L & N and are controlling in our determination that the evidence does not support the establishment of a business situs in a state other than Kentucky.

The evidence establishes that the purchase and sale of securities by the New York office are dictated by the financial needs and obligations of the L & N. The working capital of the New York office is comprised of surplus funds earned by the L & N. The New York office maintains detailed financial records of the L & N. Liquidity is a most important factor in the purchase and sale of the securities. In order to meet the day-to-day demands of the L & N, the investments are made for a period consisting of only several hours or a very few days. The entire working capital in, as well as any profits earned by, the New York office are subject to the instant demands of the L & N. The active and constant contact the domiciled corporation has with and over the New York office subjects the activities there to the control of and domination by the L & N. The L & N conducts no business as a common carrier in New York. These factors convince us that the New York enterprise is simply a convenient method of carrying on a vital and indispensable part of the company's operation as a common carrier by aiding the L & N to finance its corporate business. In our opinion the evidence requires the conclusion that while the buying and selling of securities by the L & N in New York constitute business transactions, they do not amount to a separate and independent securities business in New York. This is not to say that in order for a business to come within the integration doctrine or to have a business situs it must have no connections at all with the individual or corporation that happens to be its owner. We are saying that each case must be examined to determine if the elements present are such as to establish that the nondomiciliary business activities are a separate entity and independent from the business of the domiciled corporation.

The L & N's contention that its securities business in New York is a separate and independent business enterprise is not compatible with the position it must maintain to stay

in conformity with the Constitution of the Commonwealth of Kentucky. Section 210 of our Constitution states:

> "No corporation engaged in the business of common carrier shall, directly or indirectly, own, manage, operate or engage in any other business than that of a common carrier, or hold, own, lease or acquire, directly or indirectly, mines, factories or timber, except such as shall be necessary to carry on its business; and the general assembly shall enact laws to give effect to the provisions of this section."

Section 192 of our Constitution prohibits a corporation from engaging in any business other than that expressly authorized by its charter, and KRS 271.145(1) prohibits any corporation from engaging in any business other than that expressly authorized by its articles of incorporation.

In our opinion the L & N does have the power to buy and sell securities to facilitate its corporate purposes as a common carrier. However, consistently with the above constitutional and statutory prohibitions, the L & N cannot maintain that it is operating an independent and separate securities business having a business situs, under all this term implies, in New York or anywhere else.

It is our conclusion that the intangibles belonging to the L & N and located in its New York office did not acquire a business situs elsewhere such as to exempt them from ad valorem taxation in the Commonwealth of Kentucky.

On the cross-appeal the judgment is affirmed; on the direct appeal the cause is reversed and remanded for entry of judgment in conformity with this opinion.

All concur.

CERTIFICATE OF SERVICE

I certify that the foregoing Petition for a Writ of Certiorari was served on the other parties to this proceeding by depositing in a United States post office, with first class postage prepaid, three copies of said Petition addressed to William S. Riley, Esq., Counsel of Record for Respondent Commonwealth of Kentucky, and three copies addressed to Chairman, Kentucky Board of Tax Appeals, (it not being represented by counsel) both in Frankfort, Kentucky.

_____

Joseph L. Lenihan
Counsel for Petitioner